

**Internal Revenue Service**  
**memorandum**

date: JUN 18 1998

to: National Director  
Tax Forms and Publications Division  
Attn: Stewart Rouleau, Room 5552

from: Assistant Chief Counsel  
Office of the Associate Chief Counsel (Employee Benefits and  
Exempt Organizations)

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subject: Treatment of Advance Earned Income Credit (EIC) Payments by  
Household Employers

This is in response to your March 27, 1996, request for guidance concerning the treatment of advance EIC payments by Schedule H (Form 1040) filers in certain situations. We have reprinted your questions below. Specifically, you are interested in situations where the amount of the earned income advance payments made by the employer exceeds the employer's employment tax liability. We apologize for the delay in responding.

1. Applying Regulation 31.3507-1(c)(3) to household employment, an employer makes advance EIC payments in excess of the Schedule H, line 6, liability. Should the employer (a) recognize the excess by showing a negative figure on Form 1040, line 52, reducing the overall Form 1040 liability; or (b) request a refund procedure separate from the Form 1040 filing?

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Section 3507(a) provides, in general, that every employer making a payment of wages to an employee for whom an earned income eligibility certificate (Form W-5) is in effect shall pay the earned income advance amount to the employee at the same time as the employer pays wages to the employee.

Section 3507(d) provides that earned income advance amounts paid by an employer are not treated as the payment of compensation. Earned income advance payments are treated as made out of (i) amounts required to be deducted and withheld for the payroll period under section 3401 (relating to wage withholding), (ii) amounts required to be deducted for the payroll period under section 3102 (relating to employee FICA taxes), and (3) amounts of the taxes imposed for the payroll period under section 3111 (relating to employer FICA taxes).

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Section 31.3507-1(c)(1) of the Employment Tax Regulations provides that amounts equal to the earned income advance amount paid to employees are treated as if paid to the Treasury Department on the date on which the wages and earned income advance payments are paid to the employee. The employer must report the payment and treatment of the earned income advance payment on the employer's Form 941, 941E, 942, or 943 as the case may be. Forms 941E and 942 are obsolete. Former Form 941E filers now use Form 941. Former Form 942 filers now use Schedule H.

Section 3507(d)(2) provides that if, for any payroll period, the aggregate amount of the earned income advance payments exceeds the sum of the wage withholding, employee FICA, and employer FICA amounts, the employer shall reduce each earned income advance payment proportionately so that the aggregate amount of the earned income advance payments does not exceed the sum of the wage withholding, employee FICA, and employer FICA liability.

Section 3507(d)(3) requires the Secretary to prescribe regulations under which an employer may, in lieu of reducing the earned income advance payment, elect to pay in full all earned income advance amounts and have the additional amounts treated as the advance payment of taxes imposed by Title 26.

Under section 31.3507-1(c)(3) of the regulations, the employer reflects the election to pay the earned income advance amount in full on the employer's employment tax return. The employer must specify, with supporting computations, the excess earned income advance amounts paid and the payroll period to which the excess relates. Separate elections must be made for separate payroll periods. The excess earned income advance amount paid is treated as an advance payment of employment taxes.

Section 31.3507-1(c)(3) of the regulations further provides that the employer may claim a refund of the earned income advance amounts which exceed the employer's employment tax liability for the reporting period. The refund may be claimed on the employer's employment tax return for the reporting period. Alternatively, the excess may be applied against the employer's liability for employment taxes reported on the employer's employment tax return for the next reporting period.

Prior to the Social Security Domestic Employment Reform Act of 1994 (Pub. L. 103-387), employment taxes for household employees were reported quarterly by the employer on Form 942, Employer's Quarterly Tax Return for Household Employees. Section 2(b)(1) of that Act added section 3510 to the Code. Section 3510 changed the reporting of employment taxes on household employees to an annual basis. Employment taxes on household employees are

now reported on Schedule H, which is generally filed as part of the employer's Form 1040.

Form 1040 is now the proper form for the reporting and payment of employment taxes on household employees. Therefore, Form 1040 would generally be the proper form on which to claim a refund of any excess earned income advance payments. By showing a negative figure on Form 1040, line 52, which would reduce the employer's overall Form 1040 liability, the employer would, in effect, receive a refund.

A household employer might not be required to file Form 1040 because, for example, their income is below the threshold amount for filing an income tax return. In those cases, the Schedule H is filed separately. Household employers who file Schedule H separately should claim a refund of any excess earned income advance payments on Form 843, Claim for Refund and Request for Abatement.

2. The situation is the same as above, except the employer has a FUTA liability on Schedule H, line 25. Should the Schedule H liability (line 27) reflect the net liability (FUTA and the negative liability from line 8)?

Yes. Section 3510 applies to "domestic service employment taxes," which are defined as any FICA or FUTA taxes imposed on remuneration paid for domestic service in a private home of the employer. Congress has indicated that domestic service employment taxes should be reported on an annual basis on the Schedule H. We see no reason why the employer should not be permitted to report the net liability on line 25.

3. Beginning in 1998, employment taxes reported on Schedule H are treated as chapter 2 taxes for purposes of the estimated tax provisions (section 6654). Section 3507(d) provides that advance EIC payments are treated as payments of withholding and FICA taxes. For purposes of applying section 6654, are advance EIC payments in excess of the withholding and FICA liability (Schedule H, line 6) used to reduce the FUTA liability? Also, if a negative amount may be reported on Form 1040, line 52, is that amount used to reduce the chapter 1 taxes for purposes of section 6654?

This question is under the jurisdiction of the Office of the Assistant Chief Counsel (Income Tax & Accounting) (CC:DOM:IT&A). Accordingly, we have referred this question to them and asked them to respond directly to you.

If you have any questions, please contact Jean Casey of my office at 622-6060.

MARY E. OPPENHEIMER

By:



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